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MECHANISMS PURSUANT TO ARTICLES 6, 12 AND 17 OF THE KYOTO PROTOCOL

Synthesis of proposals by Parties on principles, modalities, rules and guidelines

Note by the Chairmen

Addendum

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PART THREE

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PART FOUR*

GLOSSARY

* Parts One, Two and Four are contained in documents FCCC/SB/1999/INF.2, FCCC/SB/1999/INF.2/Add.1, and FCCC/SB/1999/INF.2/Add.3, respectively.

I. PROPOSED PROVISIONS FOR EMISSIONS TRADING UNDER ARTICLE 17 OF THE KYOTO PROTOCOL[1]

A. Objectives, principles, purpose

1. The Alliance of Small Island States (AOSIS) believes that the design of all three mechanisms (Articles 6, 12 and 17) should firmly rest on three basic design principles:

(a) Scientific and regulatory certainty;

(b) Environmental and cost-effectiveness; and

(c) Equity between Parties. **(AOSIS)**

2. These principles should be reflected in transparent, generally applicable and clearly stated modalities, rules and guidelines that allow participants, regulators and the public at large to understand and have confidence in the operation of each mechanism. **(AOSIS)**

3. All the Protocol mechanisms should be guided by the principle of equity (Article 3.1 of the Convention; Kyoto Protocol preamble), and should be considered in the context of Article 4.4, 4.8 and 4.9 of the Convention. Equity has a role to play in both the allocation of resources generated by the mechanisms, and in respect of procedural fairness. Generally, modalities, rules and guidelines should be designed to ensure that all Parties otherwise eligible to participate should have open access to the opportunities provided by the mechanisms. **(AOSIS)**

4. However, additional incentives need to be created to attract the participation of and investment in, Parties that are often marginalized by purely market-based instruments. **(AOSIS)**

5. Transparency in the design and application of the mechanisms' rules and guidelines will be critical to achieving this access and equity. Participants, regulators and the public at large must be able to understand and have confidence in the system. **(AOSIS)**

6. AOSIS believes that robust institutions and procedures to develop, monitor and enforce these modalities, rules and guidelines will be essential to the effective operation of all the Protocol's mechanisms. **(AOSIS)**

7. It is recognized that institutional responsibilities will have to be divided, as appropriate, between new and existing bodies, at the global, regional and national levels, and, in certain circumstances, between the public and the private sector. This division of labour must be based on principles of representativeness, demonstrable competence and subsidiarity. **(AOSIS)**

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[1] Unless stated otherwise, all articles refer to the Kyoto Protocol.

8. AOSIS would not characterize the quantified emission limitation and reduction commitments as 'ambitious', since greater emission reduction commitments will undoubtedly be necessary to achieve the objective of Article 2 of the Convention. **(AOSIS)**

9. While the Protocol mechanisms may lead to substantial cost savings for some developed countries, AOSIS rejects any effort by Annex I Parties to tie their compliance with their obligations under Article 3 to the performance of what are largely untested mechanisms. AOSIS continues to endorse the conclusions of the IPCC which have identified substantial opportunities for Annex I Parties to achieve reductions more ambitious than those set out in Annex B of the Protocol through cost-effective domestic actions. **(AOSIS)**

10. Although no group of countries would be more supportive of the prompt ratification of the Protocol, AOSIS questions the usefulness of the rapid entry into force of a Protocol which has not been properly designed. **(AOSIS)**

11. The mechanisms envisaged in the Kyoto Protocol have the dual objective of ensuring that emissions reduced through these mechanisms are achieved in a manner that is both cost-effective and environmentally effective. Costs will inevitably arise from the additional domestic, regional and international oversight necessitated by the complex nature of these mechanisms. Parties should resist the pressure to make false economies in the name of cost-effectiveness. Furthermore, transactional costs of ensuring transparency and accountability should not be sacrificed for the sake of cost-effectiveness. **(AOSIS)**

12. Emissions trading is open to Annex B Parties, i.e. those with legally binding quantified emission limitation and reduction commitments. **(Australia, Canada, Iceland, Japan, New Zealand, Norway, Russian Federation, Ukraine, United States of America)**

13. The basis for emissions trading is the quantified emission limitation and reduction commitments established under Article 3. **(Australia et al.)**

14. Emissions trading shall be "supplemental to domestic actions for the purpose of meeting quantified emission limitation and reduction commitments" under Article 3. **(Australia et al.)**

15. Emissions trading does not change the combined assigned amount of Annex B Parties. **(Australia et al.)**

16. A relevant principle for further elaboration of the emissions trading regime is the principle in Article 3.3 of the Convention that policies and measures to address climate change should "be comprehensive, cover all relevant sources, sinks and reservoirs of greenhouse gases and adaptation, and comprise all economic sectors." The Protocol defines assigned amount in terms of carbon dioxide equivalence of a six-gas basket of greenhouse gases. Accordingly, a single tradable unit would be defined in terms of carbon dioxide equivalence, i.e. in units of one metric ton of carbon dioxide equivalent. **(Australia et al.)**

17. Also relevant to further elaboration of the regime is the principle in Article 3.3 that " ... policies and measures to deal with climate change should be cost-effective so as to ensure global benefits at the lowest possible cost." This principle would indicate that, while the regime needs to be sufficiently rigorous to ensure integrity (through verification, reporting, and accountability), it should also be designed to facilitate achievement of the Protocol's environmental objective at the lowest possible abatement and transaction costs. **(Australia et al.)**

18. Other principles in Article 3 of the Convention are relevant to the Protocol (and therefore indirectly to emissions trading), but have already been reflected in the Protocol's provisions, for example:

(a) The principle in Article 3.3 that "efforts to address climate change may be carried out cooperatively by interested Parties" has been reflected in several articles of the Protocol (including Articles 4, 6, 12, and 17) that permit cooperative action between and among Parties;

(b) The principle in Article 3.1 that "the Parties should protect the climate system for the benefit of present and future generations of humankind, on the basis of equity and in accordance with their common but differentiated responsibilities and respective capabilities" has been reflected to some extent in differentiated obligations both between Annex I and non-Annex I Parties and among Annex I Parties; it has also been reflected in the chapeau to Article 10 of the Protocol. **(Australia et al.)**

19. The COP is expressly authorized under Article 17 to elaborate an emissions trading regime. A Party electing to participate in such a regime must comply with the requirements of the regime. **(Australia et al.)**

20. As regards the attainment of the objectives of the Convention and the Kyoto Protocol, flexible mechanisms are merely one contribution and one link in the chain among others. It follows that joint implementation (JI), the clean development mechanism (CDM) and tradable permits (TP) cannot be dealt with separately. The quality of the final outcome depends on a comprehensive and dialectical approach. In view of the decisions of the Conference of the Parties at its fourth session which require the CDM to begin in the year 2000, the statements by Burkina Faso concern that mechanism in particular; for the sake of consistency and compatibility, they should, however, be taken into account in defining the other two mechanisms as well. **(Burkina Faso)**

21. The emissions trading under Article 17 is merely the "transfer and acquisition", between Annex B Parties, of emission reduction units (ERUs) or part of an assigned amount under Article 3.10 and 3.11. **(China)**

22. Such "transfer and acquisition" are essentially for addition and subtraction in the respective inventories of "the acquiring Parties" and "the transferring Parties", as has been clearly stipulated in Article 3.10 and 3.11, respectively. **(China)**

23. Such "transfer and acquisition" (NOT buying and selling) must be transparent and must be in compliance with the relevant provisions of the Kyoto Protocol. **(China)**

24. It is wrong to attempt to go beyond the provisions of the Kyoto Protocol to twist the "ET" under Article 17 into a so-called "market-based" international buying and selling system or regime, bringing in "brokers", etc. **(China)**

25. "Emissions trading" under Article 17 of the Kyoto Protocol shall bring about real, measurable and long-term benefits related to the mitigation of climate change. **(China)**

26. Any such trading under Article 17 and the Kyoto Protocol does not bestow rights or entitlements to Annex B Parties. **(China)**

27. The concept of "fungibility" among the three mechanisms of the Kyoto Protocol is totally unacceptable. **(China)**

28. Emissions trading shall contribute to the achievement of real and verifiable environmental benefits and cost-effectiveness. It should not lead to overall emission reductions being lower than would otherwise be the case. **(Germany on behalf of the European Community and its member States and Bulgaria, Croatia, the Czech Republic, Hungary, Latvia, Poland and Slovenia)**

29. Any part of an assigned amount transferred must correspond to the amount of actual emission reductions resulting from domestic mitigation efforts. This provision shall be subject to expert review under Article 8. **(Germany et al.)**

30. The Kyoto Protocol provides for various mechanisms in Articles 6, 12 and 17. These mechanisms may be used by Annex B Parties to assist them in part in attaining their greenhouse gas quantified emission limitation and reduction commitments under Article 3. **(India)**

31. An objective of the ongoing process is to ensure that inequities do not become entrenched. On the other hand, inequities must be reduced with a view to eliminating them. This should guide the future deliberations from which will emerge the nature and scope of the various mechanisms in Articles 6, 12 and 17. **(India)**

32. The work programme and discussions have to make a comparison of the mechanisms proposed in Articles 6, 12 and 17. The differences and similarities between the mechanisms should be brought out. Such a comparison will also facilitate an outlining of the fundamental features of the mechanisms. For this purpose, the questions raised and issues identified by the

Group of 77 and China at the subsidiary body meetings in Bonn in June 1998 (see relevant Subsidiary Bodies Misc. documents) must be addressed and elaborated upon. **(India)**

33. The Protocol has not created any asset, commodity or goods for transfers or exchange. No such assumption should be made. Neither does the Protocol create any title or entitlement. There is no provision for any concept related to inter-mechanism conveyances. **(India)**

34. Such precepts, which have the potential of constraining social and economic development and poverty eradication programmes in developing countries, must not be allowed. **(India)**

35. Historical emissions and inventories cannot bestow entitlements or any other rights of permanent benefits. **(India)**

36. The basis of trading under Article 17 needs to be addressed. The issues may be equity- or law-related. In this connection, questions related to the entitlements and rights of Parties need to be identified and elaborated. The subject relates also to the linkage between the basis of trading and any reasoning given for any entitlements and rights. Examination of this question will facilitate understanding about linked issues, including the manner of determination and mode of creation of any entitlements or rights. **(India)**

37. The design of the mechanisms must not in any way compromise the modification of longer-term trends in emissions, consistent with the objective of the Convention. The greenhouse gas reductions achieved should be real and verifiable. The mechanisms should be supplemental to domestic action. The importance of a compliance regime to ensure supplementarity must be emphasized. A well-defined process should commence for the elaboration of issues pertaining to compliance. **(India)**

38. There are methodological issues, such as determination of baselines and incrementality. These issues need to be addressed before the organizational and operational matters are looked into. **(India)**

39. Domestic legislation and systems in trading emissions are inapplicable and non-translatable for trading under Article 17. **(India)**

40. The three mechanisms need to be taken together and guided by the principle of equity, sound scientific backgrounds, environmental benefits and cost factors, as well as the shared broker principle. **(Mauritius)**

41. Parties eligible to participate must have easy access to the benefits provided by the mechanisms. Parties marginalized by solely market-based actions should be given extra incentives to attract investment. **(Mauritius)**

42. For the design and application of these mechanisms, transparency must be the keyword. Those involved with the mechanisms must be able to understand their involvement, and rules and guidelines must build up the confidence. **(Mauritius)**

43. Although clear priority should be given to the development of the CDM, Sierra Leone thinks that all mechanisms should be developed along comparable lines so that no competitive disadvantage for either of the mechanisms arises. The use of mechanisms through the countries listed in Annex B shall be supplemental to their domestic action. **(Sierra Leone)**

44. The rules and procedures for verification and certification should be the same for all flexible mechanisms in order to ensure their interchangeability. **(South Africa)**

45. The elaboration of modalities to deal with verification, certification and auditing undertaken for the CDM should be extended for use in the other flexible mechanisms. **(South Africa)**

46. The determination of baselines is an important aspect of project certification and, in view of difficulties around this issue, needs to be dealt with separately. **(South Africa)**

47. Application of relevant principles. The following principles need to be considered in defining the details of the mechanisms: equity; redress; sustainability; balanced regional activity; focus on most vulnerable developing nations; polluter pays principle; fungibility; transparency; accountability; and consistency. **(South Africa)**

48. Nature and scope of the mechanisms. All mechanisms need to contribute to the overall objective of the Convention without compromising sustainability, whilst facilitating global equity. However, their complex interactions need to be controlled and quantified to ensure appropriate behaviour is enabled. In particular the management of the outputs of the mechanisms requires careful thought. Some means of tracking the acquisition, trade, banking and application of CERs from CDM projects and ERUs developed under Articles 6 and 17 needs to be established. It is proposed that existing international entities undertake this task. Preference would be for existing entities to take on this task rather than contribute to the proliferation of international bodies. **(South Africa)**

49. Equity and transparency. The issue should not only be equity; there is also an issue of redress that is required. The mechanisms should promote the equitable allocation and consumption of global resources. **(South Africa)**

50. Equity in terms of the benefit of projects, access to projects and between non-Annex I countries should be promoted. **(South Africa)**

51. Particular attention should be paid by the COP/MOP to this issue in its review of performance. The potential for the mechanisms to compromise global equity needs to be recognized. In particular the practice of developing nations trading low-cost mitigation options

to wealthy developed nations, only for future generations to be left with the high-cost options, will merely sustain global inequity. As such, mechanisms need to be included in guidelines and procedures to avoid this problem. **(South Africa)**

52. The mechanisms should be supplemental to domestic action. However, the extent of this supplementarity is dependent on the conditions attached to the mechanisms. If developing nations are able to bank credits and activities for long-term application, the mechanisms can be used to a major extent. Failing this, the major benefits go to developed countries and the use of mechanisms should be constrained. The question of the extent to which Article 3 commitments should be achieved through domestic action should be considered on a flexible basis so that achievement of the commitment makes the most efficient use of all available mechanisms, of which domestic action is one. The question of equity will need to be discussed as well. Consideration does, however, need to be given to the introduction of flexibility in the allocations to different mechanisms, especially as a function of time and as changing technologies, development rates and cost structures present new opportunities. As such, some means of revising these allocations needs to be established. This can only be achieved if the value of the credits is comparable. In the case of the CDM the fact that the mechanism should provide for a percentage for adaptation should be built into the value so that the value of these credits is not inferior to those from the other two mechanisms. **(South Africa)**

53. Climate change effectiveness. The IPCC has already indicated that the current Kyoto Protocol targets would be inadequate to remedy any negative impacts. At the same time, it should be noted that the mechanisms will be required for all future emission reduction initiatives and as such do not only need to operate in meeting the Kyoto Protocol targets. In creating the mechanisms, the foundation for future activities is established. In evaluating climate change effectiveness through the CDM, the term reduction should be defined as reduction in increase of emissions rather than absolute reduction of emissions. Nevertheless, projects should have real, measurable and long-term benefits and effectiveness. **(South Africa)**

54. Institutional framework. The mechanisms need to operate as efficiently as possible. In this regard they should operate under normal business practices and be decentralized into individual nations where appropriate. Although a consistent mechanism needs to be established to handle CERs and ERUs, institutional arrangements for the management of the mechanisms should be flexible so as to accommodate national preferences. **(South Africa)**

55. Capacity-building. This should be an integral component of the application of the mechanisms and should include equitable capacity-building in all developing countries. **(South Africa)**

56. Adaptation. The negative impacts of climate change will have a negative impact long before mitigation measures are effective; as such, the approach to adaptation should take into account the vulnerability of countries in the following sectors: food security; energy security; disaster response; water security; flood prevention; biodiversity; spread of disease; and infrastructure development and enhancement, especially in building redundancy into

infrastructures so as to make them more robust in meeting the variability associated with climate change. **(South Africa)**

57. Linkages. The same standards should be applied to all mechanisms with respect to: units of measure (tons of CO_2-equivalent) as applied to CERs and ERUs; verification and certification of reductions; global equity; the total percentage of all three mechanisms which may be used as an offset against emission reduction targets. **(South Africa)**

58. Linkages, *inter alia*, interchangeability. Units such as CERs, ERUs and CO_2 equivalent should be equivalent and interchangeable. Consistency should apply in auditing, verification, emission reduction quantification, costing, trading, banking etc. A consistent approach to CER and ERU trading, selling, banking and application is required in order to ensure exchangeability and no value distortion. New mechanisms should not be developed for such trading. The potential role of international commodity exchanges should be investigated for this purpose. **(South Africa)**

59. The principle of primary and majority of reductions in the home country should be applied by default as the CDM develops. However, this provision should fall away if benefits to developing countries are long-term. Assurance of sustainability and non-exploitation - especially of developing nations banking, trading, selling and application of CERs and ERUs. **(South Africa)**

60. Inapplicability of Article 4.8 and 4.9 of the Convention and/or Articles 2.3 and 3.14 of the Kyoto Protocol to the mechanisms. The purpose of the CDM in addressing adaptation issues is based on a country's vulnerability to the effects of climate change as opposed to its vulnerability to the effects of implementing the Convention, which is what is covered under Article 4.8 and 4.9 of the Convention. Adaptation in terms of the CDM needs to take account of vulnerability in the sectors listed and the provisions of Articles 2.3 and 3.14. The Protocol needs to be implemented in a holistic way. It is therefore appropriate that Articles 2.3 and 3.14 are referred to when preparing rules. **(South Africa)**

61. Dependence of the ambitious environmental targets of the Kyoto Protocol upon availability of mechanisms. The IPCC should be requested to define the extent to which the mechanisms could contribute to the Kyoto Protocol and future targets. In fact, an opinion as to whether they could assist in stabilizing at 1990 levels and by when would be useful. **(South Africa)**

62. Importance of prompt decisions on workable mechanisms for ratification/entry into force. Unless substantive progress is made in the development of the rules and procedures necessary for the implementation of the Protocol very soon, the credibility of the Protocol and the Convention will be undermined amongst the nations of the world whose populations will have to consider lifestyle changes to achieve compliance with targets. The sooner the mechanisms are in place the better – especially for adaptation projects. It is proposed that early implementation of

mechanisms be defined urgently and be implemented using rules and procedures with agreement that they be reviewed on a regular basis. **(South Africa)**

63. Principle of cost-effectiveness. The principle of cost-effectiveness is supported only if it is applied holistically and in the long-term. The objective of the mechanisms should not be to achieve least-cost emission reductions. This is the primary intent of JI but not of the CDM. It should be recognized that developing countries should not be afforded the luxury of least-cost options if the high-cost options are then left to their future generations. As such, the concept of cost efficiency needs to be accompanied by some mechanism of credits for emission reductions in developing countries to be accrued by those countries for future application. **(South Africa)**

64. Role of mechanisms in promoting compliance. The mechanisms clearly increase flexibility. They should however not just be seen as low-cost options – they should contribute to sustainability and adaptation in the long term. They should also not be seen as the sole means of attaining compliance; domestic action is also critical. **(South Africa)**

65. Comparable treatment among Annex B Parties, whether using Articles 6, 12, 17 or other means to achieve their Article 3 commitments. The question of the extent to which Article 3 commitments should be achieved through domestic action should be considered on a flexible basis so that achievement of the commitment makes the most efficient use of all available mechanisms, of which domestic action is one. The question of equity will need to be discussed here as well. Consideration does, however, need to be given to the introduction of flexibility in the allocations to different mechanisms, especially as a function of time and as changing technologies, development rates and cost structures present new opportunities. As such, some means of revising these allocations needs to be established. This can only be achieved if the value of the credits is comparable. In the case of the CDM the fact that the mechanism would provide a percentage for adaptation should be built into the value so that the value of these credits is not inferior to those from the other two mechanisms. **(South Africa)**

66. Maximizing the environmental benefits of mechanisms by assuring the lowest possible cost structures. Assuring lowest cost does not necessarily mean environmental benefits; often the opposite applies unless lifecycle costs, including externalities, are considered with an attendant increase in complexity. The mechanisms clearly increase flexibility. They should however not just be seen as low-cost options – they should contribute to sustainability and adaptation in the long term. At the same time, the transaction costs of projects should be kept as low as possible. It should however be noted that this does not refer to the need to allocate proceeds to issues such as adaptation in the CDM. Transaction costs should be kept as low as possible by ensuring optimum use of existing global institutional infrastructure and refraining from establishing significant new bureaucracies to manage the mechanisms. **(South Africa)**

67. Application of any quantification of "supplemental to domestic actions" to each individual State within a regional economic integration organization. Apply as per Annex B in the Kyoto Protocol. **(South Africa)**

68. Supplementarity (concrete ceiling defined in quantitative and qualitative terms based on equitable criteria). This is understood to refer to the amount of emission reductions that may be achieved through the mechanisms. If quality is to be considered then all emissions should be calculated as CO_2 corrected for global warming potential (GWP). Quantity should not be qualified in any way. **(South Africa)**

69. Prerequisites for the use of the mechanisms (compliance, linkage with Articles 5, 7, 8). Baselines need to be in place before mechanisms can be used. **(South Africa)**

70. The foundation should be set against which performance may be measured. The rules should require compliance with targets in accordance with the approach to be agreed. Once the inventories are in place and targets are rigorously quantified, the mechanisms should be applicable with a minimum of constraints. If problems are detected, the COP/MOP should identify and address them in a spirit of flexibility and learning. **(South Africa)**

71. Articles 2.3 and 3.14. Whilst these Articles are not specifically referred to in Articles 6, 12 and 17, in the interests of minimizing duplication of effort, the requirements of these articles should be considered in structuring initiatives around the mechanisms. The Protocol needs to be implemented in a holistic way. It is therefore appropriate that Articles 2.3 and 3.14 are referred to when preparing rules. **(South Africa)**

72. Measures should be equivalent, and interchangeability across mechanisms is supported, subject to boundary conditions not being exceeded. For example, percentage allocations to mechanisms should be met. Criteria for exchange across mechanisms should be established. **(South Africa)**

73. The Kyoto Protocol mechanisms (Article 6, joint implementation; Article 12, CDM; and Article 17, emissions trading) are all aimed at enabling the Parties to meet their commitments and achieve the ultimate objective of the Convention as spelt out in its Article 2. **(Togo)**

74. First and foremost agreement must be reached on the meaning to be given to certain key words which underpin these mechanisms. These are equity, transparency, complementarity or supplementarity and technology transfer, for which clear definitions are needed to remove all ambiguity and promote a climate of mutual understanding and speedy progress in the negotiations. **(Togo)**

75. It has emerged in the negotiations that these concepts are understood differently by the group of Annex I Parties and the group of non-Annex I Parties. **(Togo)**

76. We consider that all the flexibility mechanisms should be handled in a concerted manner, and not separately. It is obvious that the global approach of a single market for emissions trading in which all countries can participate modifies the order of the technical aspects to be settled. All the emission credit trading mechanisms must be subject to the same type of levy. **(Togo)**

77. Although the "Buenos Aires Plan of Action" focuses on a number of important points, the analyses and discussions on the mechanisms should move forward in a harmonious rather than a compartmentalized way. **(Togo)**

78. The climate change problem is a global one, and the fact that responsibilities are common but differentiated means that the non-Annex I Parties should not be confined solely to the debate on the CDM designed for them, while the Annex I Parties work together and devise structures for the other mechanisms (activities implemented jointly, emissions trading). **(Togo)**

79. Togo is convinced that the world market for emissions trading involves everyone and that the Kyoto Protocol flexibility mechanisms are by no means the solution to the problems of climate change. **(Togo)**

80. The effectiveness of the flexibility mechanisms rests on the commitment of the Annex I Parties to pursue all the domestic policies and measures needed to comply with their commitments under the Convention and the Protocol. The Buenos Aires Plan of Action provides no indication as to the means of demonstrating progress as stipulated in Article 3.2 of the Protocol. These indicators therefore need to be examined before the year 2000. **(Togo)**

81. Each of the flexibility mechanisms rests on market principles, i.e. on trading emission rights for cash. The success of the flexibility mechanisms will depend on the drawing up of rules of allocation, which, on grounds of equity and transparency, should be based on the principle of an equal right for each individual on the planet, whether he or she falls under Annex I or not. **(Togo)**

82. Uganda believes that the design of the flexible mechanisms must be based on strong global environmental benefits and sustainable development principles, taking into account equity and transparency considerations. The design of the three flexible mechanisms should also take into account simplicity, transparency and easy to apply procedures to ensure successful implementation of the flexible mechanism and attainment of global environmental benefit. **(Uganda)**

83. Irrespective of the form the CDM takes, the same rules, procedures and principles must be applied to the other flexible mechanisms, where applicable, to ensure credibility and quality of the credits. **(Uganda)**

84. The design of the CDM and implementation modalities of the other two flexible mechanisms must be based on equity principles to ensure fairness to all humans now and for generations to come. The present generation should not and must not continue to deprive the future generations. The imbalance between the present generations and future generations must be addressed. It is equally very important to address the environmental and social imbalances. In attempting to address the present imbalances, the principle of equity must be applied to ensure equitable distribution of resources under the flexible mechanisms. Due consideration must be given to the following:

(a) Inter- and intra-generation

(b) North to North

(c) North to South

(d) South to South

(e) Within subregions

The principle of equity can only be seen to be applied if the process of implementing the three flexible mechanisms is transparent to all Parties and interested Parties including the private sector. The rules of the game must be laid down on the table in simple and clear language. Developing country Parties, particularly the African Parties, must be assisted to build capacity to ensure that transparent and simple rules are developed at the national level. **(Uganda)**

85. The principle of cost-effectiveness should not be viewed from the window of the developed country Parties but from a holistic view point. The market forces are not perfect and therefore if left to the market forces, cost-effectiveness will be biased towards the investor. In order to take on board the view of developing country Parties the so-called market forces must be regulated. This again calls for transparency in the design of the modalities and procedures for implementing the flexible mechanisms. **(Uganda)**

86. The establishment of the flexible mechanisms of the Kyoto Protocol presupposes the deepening of the Parties co-operation in the fulfilment of their obligations and improvement of the effectiveness of the national activities. Such co-operation can be carried out on the basis of partnership, understanding of the national ecological and economical problems, absence of discrimination, and can be strengthened by the participation of the donor governments and governments-investors. **(Uzbekistan)**

87. Simple, effective and clear rules should guide these mechanisms. Such rules should be credible and agreed upon. Nothing in the documents on these mechanisms should be treated as to diminish or damage the responsibilities and duties of Annex I Parties in accordance with the Convention. **(Uzbekistan)**

88. The framework and function of all three mechanisms should be clearly identified to guarantee the confidence of governments, agencies, and investors involved, in the interest of their participation in the activities on such mechanisms, and of additional financing from the state and private sector. **(Uzbekistan)**

B. Role of the COP and/or the COP/MOP

89. The global framework must be presided over by the COP/MOP, as the supreme body of the regime, and any smaller bodies authorized to carry out executive functions on behalf of the COP/MOP, must have a membership that reflects the unique representational balance established by the practice of the Parties (such as the COP Bureau). **(AOSIS)**

90. AOSIS strongly supports the principle that arrangements made among subsets of Parties, including within regional economic integration organizations, should be subject to the oversight of, and be accountable to, the COP/MOP. **(AOSIS)**

91. Verification and auditing entities are to be defined by the COP/MOP or as delegated by the COP/MOP but should include private sector entities. **(South Africa)**

92. The COP/MOP should carefully track the potential for distortion of competition and include standard checks in the guidelines. **(South Africa)**

C. Parties

93. AOSIS believes that the existence of the capacity must be demonstrated as a prerequisite for participating in the mechanisms, and that resources should be made available to eligible Parties to meet the costs of building such capacity. **(AOSIS)**

94. Requirements for participation by Parties in emissions trading should be structured so as to both:

(a) Bolster the credibility of the emissions trading regime itself; and

(b) Promote compliance with other key elements of the Protocol. **(Australia et al.)**

95. In terms of bolstering the environmental credibility of the trading regime, Article 17 places critical importance on verification, reporting, and accountability. These goals would be well served by providing that a Party could not participate in emissions trading under Article 17 if it were found either:

(a) Not to be maintaining a national registry meeting specific criteria in accordance with the provisions of this Annex)see document FCCC/SB/1999/MISC.3/Add.1; or

(b) Not to be in compliance with its obligations under Articles 5 and 7 of the Protocol. **(Australia et al.)**

96. Linking participation in the emissions trading regime with compliance with Articles 5 and 7 would have the ancillary benefit of promoting compliance with key obligations under the Protocol. It is through these articles that Parties will demonstrate compliance with their

quantified emission limitation and reduction commitments. Assessing compliance with such commitments indeed depends upon proper implementation of these articles. **(Australia et al.)**

97. If a Party's consistency with the requirements in paragraph 94 (a) or (b) above is called into question [by the review process under Article 8?][other?], the issue will be expeditiously resolved [through a general procedure applicable to the Protocol][through a specialized procedure]. **(Australia et al.)**

98. Concerning potential challenges to a Party's implementation of the requirements for participation, the following aspects should be considered:

(a) Who can call into question a Party's consistency with the requirements for participation? The expert review process under Article 8 can raise questions about a Party's implementation; also under Article 8, Parties can bring questions about implementation to the attention of the COP/MOP.

(b) What procedure will be used to decide whether a challenged Party is not meeting the eligibility requirements for participation? Expert review teams are not authorized under Article 8 to make determinations concerning compliance or non-compliance. Therefore, a procedure would be necessary to make such determinations and, as appropriate, identify necessary steps for a Party to restore its eligibility. The procedure might be the same procedure applicable to the rest of the Protocol or a specialized procedure (perhaps even a subset of the more general procedure). It would appear that, in any event, the procedure would need to be expeditious.

(c) Will de minimus inconsistencies with the requirements for participation need to be addressed? **(Australia et al.)**

99. Each Party participating in emissions trading shall include in its annual submission to the Secretariat under Article 7, *inter alia*, information, in a standard electronic format, on:

(a) Transfers and acquisitions of units of assigned amount during that year, including, for each unit, the serial number and the Party's registry to which it was transferred or from which it was acquired;

(b) Any units of assigned amount (identified by serial number) that have been retired. **(Australia et al.)**

100. "Emissions trading" under Article 17 shall be conducted between or among the Parties included in Annex B to the Protocol. **(China)**

101. Parties included in Annex B shall be eligible to "transfer" or "acquire" part of the assigned amount, if they:

(a) Are in compliance with Articles 3, 5, and 7, and are responsible for meeting their commitments under the Kyoto Protocol;

(b) Are not in violation of the compliance Article, namely Article 18;

(c) Have a transparent national system for recording and verification of such "transfers" and "acquisitions". **(China)**

102. A Party included in Annex B shall be eligible to transfer or acquire any part of an assigned amount under the provisions of Article 17, if the Party:

(a) Has ratified the Kyoto Protocol;

(b) Is bound by a compliance regime adopted by the COP/MOP;

(c) Has not been excluded from participation in emissions trading according to the procedures and mechanisms under the compliance regime mentioned above;

(d) Is in compliance with the provisions of Articles 5 and 7 of the Kyoto Protocol and Article 12 of the Convention. **(Germany et al.)**

103. Any Party participating in emissions trading under Article 17, or authorizing any legal entity to participate in emissions trading under the provisions of paragraphs 120-121 below, shall include in its inventory to be submitted to the secretariat under Article 7.1, information on any part of an assigned amount added to or removed from its national registry during the relevant year, including the serial number for each unit and the Party to which it was transferred or from which it was acquired. **(Germany et al.)**

104. The secretariat shall include information submitted under paragraph 103 above in its annual compilation and accounting of emissions inventories and assigned amounts under Article 8. **(Germany et al.)**

105. [...][2] **(Germany et al.)**

106. Considering that the mechanisms constitute a voluntary and cost-effective modality for Annex I countries to reduce their emissions, they can benefit from the use of the mechanisms only if they are in compliance with the reduction commitments established under the Convention as well as in the Protocol. **(Peru)**

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[2] Text will be provided at a later stage.

107. Basis of rights and entitlements for emissions trading of Parties included in Annex B. According to Article 17, all can trade subject to meeting the requirements of the Convention and the Kyoto Protocol, as well as verification issues. **(South Africa)**

108. Prerequisites for the use of Article 17 (compliance, linkage with Articles 5, 7 and 8). The foundation should be set against which performance may be measured. Once the inventories are in place and targets are rigorously quantified, the mechanism should be applicable with a minimum of constraints. Meaningful progress in domestic action could be considered as a prerequisite, but this would require careful definition. If problems are detected then the COP/MOP should identify and address them in a spirit of flexibility and learning. **(South Africa)**

109. Accessibility. Accessible to all Annex B Parties. **(South Africa)**

110. Determination and creation of rights and entitlements for emissions trading of Parties included in Annex B. All should be entitled to trade, in accordance with Article 17. **(South Africa)**

111. Assigned amounts can be traded as long as the transacting Parties can demonstrate compliance. **(South Africa)**

112. Eligibility (e.g. links to Articles 5 and 7). The foundation should be set against which performance may be measured. Once the inventories are in place and targets are rigorously quantified, the mechanism should be applicable with a minimum of constraints. Meaningful progress in domestic action could be considered as a prerequisite, however this would require careful definition. If problems are detected then the COP/MOP should identify and address them in a spirit of flexibility and learning. **(South Africa)**

113. Matters relating to verification, reporting and accountability. As per standard practice against standards and methodologies to be developed. Reporting on transfers and acquisitions in assigned amounts to be undertaken in national communication as well as the entity managing trades etc. **(South Africa)**

114. Switzerland believes that, for each of the three Kyoto Protocol Mechanisms, there is a need for independent validation/certification. Under Article 6, each project must be validated to ensure that it meets the project eligibility criteria and has a baseline that meets agreed standards, and the resulting emission reductions must be certified after they have occurred. The same basic validation/certification requirements generally hold true for Article 12, as well. Under Article 17, the national systems for the preparation of emission inventories must be validated[3] to conform with the guidelines to be decided upon by the COP/MOP and, in the case that legal entities are

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[3] It is essential for the credibility of the emissions trading system that national emission inventory systems/data be validated by an accredited independent instance. Otherwise there is huge room for falsification of inventory data, since uncertainties of 50-100 per cent or more are not uncommon.

authorized to participate in emissions trading, national systems for accurate tracking and accountability of trading activities by legal entities must also be validated to ensure that they meet the requirements to be specified under the rules for Article 17. Furthermore the amount of excess PAA units available to a Party must be certified, and certificates issued annually (assuming a post-verification trading system). **(Switzerland)**

115. Building on existing know-how and institutions, the generally local independent "operational entities" (borrowing the terminology from the Kyoto Protocol for the CDM) could be accredited to perform the necessary validations/certifications by existing national or regional accreditation authorities designated by the COP/MOP. In the case of the CDM, Article 12.5 states that the operational entities are to be designated by the COP/ MOP, but this "designation" could occur via national/regional accreditation authorities to avoid an administrative bottleneck. Discussion of this and other possible approaches would be welcome at the upcoming sessions of SBSTA/SBI. For the other mechanisms, operational entities are not explicitly mentioned, but will be needed if validation/certification is required, as proposed above. **(Switzerland)**

116. Operational entities must be accredited by designated national/regional authorities to perform validation/certification on the basis of a set of protocols (or standards) for validation or certification. These validation and certification protocols must by adopted by the COP/MOP. In the case of emissions trading and joint implementation, the secretariat might be given the task of actually issuing certificates based on the certification report by the operating entity, whereas this task might be performed by the executive board under the CDM. **(Switzerland)**

117. If such a system is established, it would only apply to those Parties that choose to engage in the Kyoto Protocol Mechanisms, and would have to be linked to the entire system for measurement, reporting, review and compliance under the Protocol (including the expert review process under Article 8, which applies only to Annex I countries). The review process in Article 8.1 and the expert reviews under Article 8.2 might be used to spot-check the performance of the operational entities acting in those Annex I Parties engaging in JI, CDM or emissions trading. The Article 8 reviews, however, could not replace the verification/certification process for the Kyoto Protocol mechanisms. **(Switzerland)**

D. Legal entities

118. It is at the discretion of each Party whether legal entities (e.g. private firms, non-governmental organizations, individuals) are allowed to trade. Having more players in the system is likely to mitigate concerns about market power. **(Australia et al.)**

119. A Party that authorizes its legal entities (e.g., private firms, non-governmental organizations, individuals) to transfer or acquire units of assigned amount shall ensure that such participation is consistent with the emissions trading regime referred to in this Annex (see document FCCC/SB/1999/MISC.3/Add.1). Further, such Party shall remain responsible for fulfilment of its obligations under the Protocol (i.e. they cannot be delegated). **(Australia et al.)**

120. A Party included in Annex B may authorize legal entities to participate in emissions trading under its responsibility, in accordance with the rules set out in paragraphs 6 to 10 of the submission (see document FCCC/SB/1999/MISC.3), if the Party:

(a) Is in compliance with the provisions of paragraph 102 above;

(b) Has established and maintains a national system for accurate monitoring, verification, accountability and allocation of parts of assigned amount to any legal entity it chooses to authorize. Guidelines on the establishment, maintenance and international compatibility of these national systems are to be elaborated in a separate appendix to these principles, modalities, rules and guidelines. **(Germany et al.)**

121. Participation of legal entities in emissions trading under Article 17 does not affect the responsibility of the Parties included in Annex B for the fulfilment of their commitments under the Kyoto Protocol. **(Germany et al.)**

122. Legal entities as identified by the participating governments and the COP/MOP should be able to freely participate in the roles identified. **(South Africa)**

123. Legal entities are to be defined in the guidelines. Generally, entities should be defined by participating governments at their discretion. **(South Africa)**

E. Definition of units

124. AOSIS has repeatedly stressed that any modalities, rules and guidelines developed for the Protocol's mechanisms must aim to ensure, as their primary objective, that combined emission reduction obligations reflected in Annex B are not undermined. This requires the setting of rules that ensure the effective equivalence in quality of any parts of assigned amount (PAA), emissions reductions units (ERUs) and certified emissions reductions (CERs) that are allowed to be exchanged through the Protocol's mechanisms. **(AOSIS)**

125. AOSIS believes that in order to preserve the environmental effectiveness of the commitments agreed in the Kyoto Protocol, Parties should be able to exchange parts of assigned amount only under circumstances in which the emission reductions involved meet standard and harmonized criteria. Any PAA, CER or ERU entering into the system should be clearly identified by its emissions value, date and country of origin. The value of any allowance or offset traded should depend on the ability of the issuer of the allowance or offset to demonstrate the genuineness of the emission reductions it represents. **(AOSIS)**

126. For the sake of simplicity, and in order to promote compatibility among Protocol mechanisms, a tradable unit would be defined. **(Australia et al.)**

127. That which is being traded is assigned amount, which derives from initial assigned amounts under Article 3.7 and Annex B, as adjusted under other provisions of Article 3. **(Australia et al.)**

128. Transfers and acquisitions should be made in discrete units of assigned amount. **(Australia et al.)**

129. To take account of the comprehensive six-gas approach, the tradable unit would be one metric ton of CO_2-equivalent, calculated using the global warming potentials (GWPs) defined by decision 2/CP.3. If those GWPs are subsequently revised in accordance with Article 5, the revised GWPs would apply. **(Australia et al.)**

130. Units of assigned amount would be issued by a Party and, to promote tracking and accountability, should be identified by a unique serial number that includes the Party of origin and the commitment period for which the units are issued. (Units of assigned amount may be banked for use in future commitment periods pursuant to Article 3.13.) **(Australia et al.)**

131. Transfers and acquisitions of assigned amount (derived from initial assigned amounts under Article 3.7, as adjusted under other provisions of Article 3) shall be made in units of assigned amount of one metric tonne of CO_2 equivalent (calculated using the global warming potentials defined by decision 2/CP.3 or as subsequently revised in accordance with Article 5) issued by a Party and identified by a unique serial number that includes the Party of origin and the commitment period for which the units are issued. (Units of assigned amount may be banked for use in future commitment periods pursuant to Article 3.13.). **(Australia et al.)**

132. The concept of "fungibility" among the three mechanisms of the Kyoto Protocol is totally unacceptable. **(China)**

133. Transfers and acquisitions of any part of an assigned amount (PAA) by a Party or legal entity that the Party has authorized to participate under its responsibility, shall be denominated in units of one metric ton of carbon dioxide equivalent calculated using the global warming potentials defined by decision 2/CP.3 or as subsequently revised in accordance with Article 5. **(Germany et al.)**

134. Each PAA unit shall be identified by a unique serial number that indicates its Party of origin and its associated commitment period. **(Germany et al.)**

135. An invalidated PAA unit, as referred to in paragraphs 191-194 below, cannot be used to meet any Party's commitment under Article 3, and cannot be further transferred or acquired. **(Germany et al.)**

136. The price of ERUs should be equivalent to ERUs under Article 6 and CERs under Article 12. **(South Africa)**

137. The tradable unit should be the ERU, measured in tons of CO_2-equivalent (as defined by IPCC constants), which is the same ERU defined under Article 6 and which is equivalent to a CER defined under Article 12. **(South Africa)**

138. Fungibility among mechanisms. Measures should be equivalent, and interchangeability across mechanisms is supported – subject to boundary conditions not being exceeded. For example, percentage allocations to mechanisms should be met. Criteria for exchange across mechanisms should be established. **(South Africa)**

F. Verification

139. Participants in any transaction must be able to demonstrate the genuineness of any allowance or offset before it can be added to or subtracted from an assigned amount. **(AOSIS)**

140. AOSIS believes that the effective operation of the mechanism's and Protocol's procedures for reporting, monitoring and verification are inextricably interlinked. Before an emission reduction unit generated in any Party can be offset against any part of an amount assigned to any other Party, the rules adopted under Articles 4, 6, 12 or 17 for verification, reporting and accountability must provide a basis for demonstrating that the regulatory mechanisms in place in both Parties are effective. **(AOSIS)**

141. The rules for verification, reporting and non-compliance and accountability should either be harmonized between the participating States at the domestic level, or the intervention of regional or international rules with equivalent 'bite' will be necessary. Furthermore, because there will be a shared, global interest of all Parties to ensure that arrangements between two or more Parties are jointly achieving the relevant part of an assigned amount, the Protocol must provide multilateral oversight to ensure verification, reporting and accountability. **(AOSIS)**

142. Real and verifiable reduction of greenhouse gas emissions. These should be defined as per verification and auditing procedures. A trade cannot be permitted unless the ERUs are first verified. **(South Africa)**

143. Matters relating to verification, reporting and accountability. According to standard practice against standards and methodologies to be developed. Reporting to be undertaken in national communication as well as the entity managing trades etc. **(South Africa)**

144. Transparency should be assured via verification, auditing and reporting as per normal certification practice against standards and methodologies to be developed by the COP/MOP. **(South Africa)**

145. Switzerland believes that – for each of the three Kyoto Protocol Mechanisms, there is a need for independent validation/certification. **(Switzerland)**

146. Under Article 17, the national systems for the preparation of emission inventories must be validated[4] to conform with the guidelines to be decided upon by the COP/MOP and, in the case that legal entities are authorized to participate in emissions trading, national systems for accurate tracking and accountability of trading activities by legal entities must also be validated to ensure that they meet the requirements to be specified under the rules for Article 17. Furthermore the amount of excess PAA units available to a Party must be certified, and certificates issued annually (assuming a post-verification trading system). **(Switzerland)**

147. For this mechanism, operational entities are not explicitly mentioned, but will be needed if validation/certification is required. **(Switzerland)**

148. Operational entities must be accredited by designated national/regional authorities to perform validation/certification on the basis of a set of protocols (or standards) for validation or certification. These validation and certification protocols must be adopted by the COP/MOP. In the case of emissions trading and joint implementation, the Secretariat might be given the task of actually issuing certificates based on the certification report by the operating entity, whereas this task might be performed under the CDM by the executive board. **(Switzerland)**

G. Registry

149. A participating Party would be required to maintain a national registry containing records of all holdings, transfers, and acquisitions of units of assigned amount by that Party and any legal entities authorized by it. **(Australia et al.)**

150. Information held by a registry should be publicly accessible. **(Australia et al.)**

151. Transfers and acquisitions of units of assigned amount would be made by removing units (identified by serial number) from the registry of the transferring Party and adding them to the registry of the acquiring Party. **(Australia et al.)**

152. If a Party uses a unit of assigned amount towards meeting its quantified emission limitation and reduction commitment, it would retire that unit, in which case such unit would not be able to be further used or transferred; a record of all retired units of assigned amount would be kept by the Party in its registry. **(Australia et al.)**

153. To simplify international transactions, two or more Parties would be able to voluntarily maintain their registries within a consolidated system. **(Australia et al.)**

154. Any two or more Parties may voluntarily maintain their registries in a consolidated system, within which each registry would remain legally distinct. **(Australia et al.)**

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[4] It is essential for the credibility of the emissions trading system that national emission inventory systems/data be validated by an accredited independent instance. Otherwise there is huge room for falsification of inventory data, since uncertainties of 50-100 per cent or more are not uncommon.

155. To simplify tracking and reporting requirements of various Kyoto Protocol mechanisms, a Party might choose to use one registry for more than one mechanism. **(Australia et al.)**

156. National registries should be based on compatible systems for electronic record-keeping and reporting. Development of guidelines on this matter should be further considered. **(Australia et al.)**

157. Any Party included in Annex B participating in emissions trading under Article 17 or authorising any legal entity to participate in emissions trading under the provisions of paragraphs 120-121 above, shall establish and maintain a national registry which accurately records all holdings, transfers, and acquisitions of any part of an assigned amount by the Party and its authorized legal entities. Information maintained in such a national registry shall be publicly accessible. **(Germany et al.)**

158. Guidelines on the establishment, maintenance and international compatibility of national registries are to be elaborated in a separate appendix. **(Germany et al.)**

159. Article 17 provides that each Annex B Party may transfer any part of its assigned amount to any other Annex B Party. Under Article 3, these transfers are added to or subtracted from a Party's initial assigned amount. **(New Zealand)**

160. An essential building block of a trading system is a mechanism for recording transfers of portions of a Party's assigned amount. To meet this need, the trading rules under Article 17 should require each Party that elects to trade to establish and maintain a national registry. The registry would record who holds each part of assigned amount (an "assigned amount unit" or "AAU"[5]), and track all transfers and acquisitions of such AAUs prior to their use for compliance. **(New Zealand)**

161. National registries are needed for several important reasons. Each Annex B Party will need a tracking system to keep an official record of trade-related increases and decreases in the assigned amount held by the Party or by legal entities operating under its responsibility. A Party's registry will serve as the starting point for determining compliance with Article 3 commitments (together with measurement and reporting of information pursuant to Articles 5 and 7). Registry information will provide evidence that a selling Party or one of its entities possesses an AAU that it offers for sale. Likewise, buyers will use registries to record and confirm the official transfer of AAUs from seller to buyer. A system of compatible national registries will facilitate transaction efficiency and promote compliance, as well as help build public confidence in emissions trading. **(New Zealand)**

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[5] An AAU is the tradable unit of a Party's assigned amount. AAUs have also been termed parts of assigned amount (PAA).

162. While national registries are likely to be most frequently used for emissions trading, they will play an equally important role for joint implementation (Article 6) and the clean development mechanism (Article 12), and may be helpful in accounting for reallocations of assigned amounts under Article 4. Transfers of assigned amount under Article 6 will need to be tracked to ensure an offsetting adjustment takes place. Pursuant to Article 3.12, certified emission reduction units from the CDM can be added to a Party's assigned amount and, therefore, subsequently traded. These transactions will also need to be tracked. The concept of national registries and their operation should therefore not be considered solely in an emissions trading context, but in the much broader context of Articles 3, 4, 6, 12, and 17.[6] **(New Zealand)**

163. Some central register is going to have to be kept at national level with some form of roll-up to international level. It is proposed that existing institutional mechanisms for trading and banking commodities should be investigated as the basis for tracking the creation, trading and banking of CERs and ERUs. This function may also be undertaken by national central banks or similar institutions. The same institution should be used for all mechanisms. For developing countries this would typically only apply to the CDM. However, developed nations would also need to include ERUs developed under Articles 6 and 17. **(South Africa)**

164. A mechanism needs to be put in place to determine who holds valid ERUs at any one time, both to track the performance of the mechanism and to define compliance with such targets as Kyoto Protocol targets. This entity may be a national central bank or similar organization. For developing countries this would typically only apply to the CDM, but developed countries would also need to include ERUs developed under Articles 6 and 17. Reporting should be undertaken in the national communication as well as the entity managing trades etc. **(South Africa)**

H. International reporting

165. There would be an annual international synthesis of the Parties' annual reports concerning emissions trading. Such a synthesis would serve a number of functions, including:

(a) At the end of a commitment period, they would be relevant to the assessment of compliance with target obligations;

(b) During a commitment period, they would assist in tracking units of assigned amount traded between Parties' registries or retired; and

(c) In general, they would help reveal discrepancies in the recording of transfers of assigned amount by cross-checking Parties' submissions (a verification function). In the event of discrepancies in the reports submitted by Parties, the relevant Parties would have the opportunity to investigate and correct such discrepancies. **(Australia et al.)**

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[6] The full text of this submission is contained in document FCCC/SB/1999/MISC.3.

166. The secretariat would prepare such a synthesis as part of the annual compilation and accounting of emissions inventories and assigned amounts under Article 8. **(Australia et al.)**

167. Such a synthesis, which should be publicly available, would identify transfers and acquisitions of units of assigned amount during that year between Parties' registries and which units of assigned amount have been used by a Party for purposes of compliance with its quantified emission limitation and reduction commitment. **(Australia et al.)**

168. The secretariat, as part of the annual compilation and accounting of emissions inventories and assigned amounts under Article 8, shall present a publicly-available synthesis of the reports by Parties on transfers and acquisitions of units of assigned amount during such year, including which units have been used by a Party for purposes of compliance with Article 3.1. It shall provide Parties the opportunity to investigate and correct any discrepancies in the recording of transfers of assigned amount. The synthesis shall reflect any remaining discrepancies. **(Australia et al.)**

169. Any Party participating in emissions trading under Article 17, or authorizing any legal entity to participate in emissions trading under the provisions of paragraphs 120-121 above, shall include in its inventory to be submitted to the secretariat under Article 7.1, information on any part of an assigned amount added to or removed from its national registry during the relevant year, including the serial number for each unit and the Party to which it was transferred or from which it was acquired. **(Germany et al.)**

170. The secretariat shall include information submitted under paragraph 169 above in its annual compilation and accounting of emissions inventories and assigned amounts under Article 8. **(Germany et al.)**

I. Competitiveness

171. Depending upon further consideration and discussions with other Parties, there may be a need to address additional issues in the elaboration of the emissions trading regime, such as competition. **(Australia et al.)**

172. The COP/MOP should carefully track the potential for distortion of competition and include standard checks in the guidelines. **(South Africa)**

J. Market size and structure

173. Any part of an assigned amount transferred must correspond to the amount of actual emission reductions resulting from domestic mitigation efforts. This provision shall be subject to expert review under Article 8. **(Germany et al.)**

174. The use of "hot air" is permitted subject to limitations on the extent of application of this mechanism and the ruling price of ERUs and CERs. **(South Africa)**

175. Lack of authority to elaborate "supplemental to domestic actions"; inadvisability of doing so. It is desirable to include domestic action to avoid exploitation of short-term opportunities, especially in economies in transition, in exchange for long-term high costs. As such, the mechanisms should be supplemental to domestic action. However, the extent of this supplementarity is dependent on the conditions attached to the mechanisms. If developing countries are able to bank credits and activities for long-term application, the mechanisms can be used to a major extent. Failing this, the major benefits go to developed countries and the use of mechanisms should be constrained. **(South Africa)**

K. Relationship to domestic policies

176. Domestic legislation and systems in trading emissions are inapplicable and non-translatable for trading under Article 17. **(India)**

L. Relationship to Article 4

177. Particular issues arise when considering the relationship between the emissions trading regime and Article 4. **(Australia et al.)**

178. If Parties are not able to participate in emissions trading because they are not in compliance with Articles 5 and 7, the question arises as to how such a requirement would apply to Parties operating under Article 4. Specifically, if a Party operating under an Article 4 agreement wished to participate in emissions trading, would all Parties operating under that agreement need to be in compliance with Articles 5 and 7? It would appear so, because transfers or acquisitions by any one such Party would affect compliance with the total combined quantitative commitment of all such Parties. **(Australia et al.)**

M. Levies

179. AOSIS believes strongly that adaptation surcharges should be assessed against all transactions eligible under the Protocol's mechanisms. The principle of common but differentiated responsibilities, and the obligation in Article 4.4 of the Convention, provide sufficient basis for ensuring that those mechanisms open only to Annex I Parties should share the responsibility of generating adaptation resources. AOSIS believes that the concerns of some Parties that high surcharges will dampen the market's interest in the mechanisms can be answered by agreeing a range of charges that could be adjusted by the COP/MOP and/or the executive board of the CDM in response to market signals. **(AOSIS)**

180. It would be beneficial and realistic if the collection of funds from certified project activities referred to in Article 12, paragraph 8, concerned all three flexible mechanisms so as to increase the amount available to cover administrative expenses and vulnerable developing countries' costs of adaptation. Adaptation projects in the least developed countries will require substantial investments beyond the capacity of the CDM alone. With that in mind, adaptation

and administrative expenses should be funded by a levy of 15 per cent per mechanism. The Parties should be guided in drawing up projects by criteria consistent with the objectives set out in Article 12, paragraph 2. **(Burkina Faso)**

181. In consideration of Article 12.8, sources of funds for adaptation projects should include the following:

(a) A tax on each of the three mechanisms: joint implementation, clean development mechanism (Article 12) and emissions trading (Article 17) to fund adaptation projects, and thus foster sustainable development in developing countries, particularly in Africa;

(b) A tax on bunker fuels; and

(c) A non-compliance fine on Annex I Parties. **(The Gambia)**

182. All of the Kyoto Protocol mechanisms: emissions trading, joint implementation and the clean development mechanism, shall contribute with a percentage of the transactions' value to meet the adaptation needs of developing countries. These contributions will be applied exclusively to finance adaptation costs originating in the adverse effects of climate change in developing countries, prioritizing the imminent damages to human lives (famine, epidemics, etc) and assistance operations (rescues of unexpected magnitude or character climate phenomena victims). **(Peru)**

183. In order to create a level playing-field, it is of the utmost importance that a fee is levied not only on the CDM but also on emissions trading and joint implementation, and put into an adaptation fund. This fee could be part of the administrative fee that accrues for writing or trading a CER or ERU, or whatever is decided to be a tradable unit. An adaptation fund should be established. **(Sierra Leone)**

184. Lack of authority to impose a charge for adaptation. This is not an issue under Article 17 if the CDM is adequately structured to cater for adaptation projects and the appropriate level of funding being allocated to these projects in all developing countries. **(South Africa)**

185. Togo suggests that the adaptation fund should be extended to all the flexibility mechanisms proposed under the Kyoto Protocol. **(Togo)**

186. Uganda proposes that adaptation be funded from the following:-

(a) Adaptation cost be met from all the three flexible mechanisms of the Kyoto Protocol;

(b) A portion of monies accruing from measures taken by Annex I Parties to mitigate GHG emissions be channelled to meet adaptation costs;

(c) Non-compliance penalties;

(d) Voluntary contributions from Parties, multilateral agencies and other sources. **(Uganda)**

N. Liability for sales of non-surplus units

187. Another issue is how to address the case where the emissions of a Party that transferred assigned amount under emissions trading exceed its assigned amount. (This issue has been called the issue of "buyer/seller liability," but is more accurately referred to as an "allocation of risk" issue). In general, there should be consistent treatment of Parties whose emissions exceed their assigned amounts, whether or not they had engaged in emissions trading.

(a) It should be noted, in this regard, that Article 4 incorporates the so-called "seller liability" approach. Specifically, under an Article 4 allocation agreement, Party X in effect gives a certain portion of its assigned amount to Party Y. Assuming the Parties exceed their aggregate emission level, Article 4.5 provides that each Party is responsible for its own level of emissions set out in the allocation agreement. If Party X exceeds its individual reallocated level (i.e., it gave to Party Y some of the assigned amount that it needed to cover its own emissions), only Party X would face whatever consequence applies generally to Parties that exceed their targets; Party Y would not have to return the assigned amount that it received under the allocation agreement in order to bring Party X back into compliance. **(Australia et al.)**

188. Need to address issue of whether a Party whose emissions (after the short period) exceeded its assigned amount for the previous commitment period should retain its eligibility to participate in emissions trading under Article 17 in the subsequent commitment period. **(Australia et al.)**

189. These end-of-commitment-period issues merit further consideration, taking into account discussions on the overall non-compliance regime. **(Australia et al.)**

190. "Transfers" of any emission reduction units or part of an assigned amount by a Party included in Annex B to another Party would be valid only if it is reported and verified that the former would have fulfilled its commitments under Article 3, in accordance with the rules and guidelines to be decided by the Conference of the Parties. **(China)**

191. Option 1 - Shared liability:

(a) If a Party is found to be in non-compliance with its commitments under Article 3, a portion [x%] of any of its assigned amount that has been transferred to other Parties under the provisions of Article 17, shall be invalidated and cannot be used for the purpose of meeting commitments under Article 3 or further traded. [The portion [x%] to be invalidated shall be some multiple of the degree of non-compliance. The degree of non-compliance is the percentage difference between emissions in the commitment period and assigned amount.] **(Germany et al.)**

192. Option 2 - compliance reserve:

(a) A portion [x%] of every transfer under Article 17 shall be placed in a compliance reserve in which event the units may not be used or traded. The secretariat, as part of the annual compilation and accounting of emissions inventories and assigned amounts under Article 8, shall include a report of the units deposited in the compliance reserve. At the end of the commitment period, such units shall be returned to the Party of origin if that Party is in compliance with its commitments under Article 3, in which case the units can be transferred or banked for future commitment periods. If at the end of the commitment period a Party is not in compliance with its commitments under Article 3 an appropriate number of units deposited in the reserve account shall be invalidated in which case they may not be further used or traded. **(Germany et al.)**

193. Option 3 - "Trigger":

(a) If a question is raised on a Party's compliance with its commitments under Article 3 and the Party is subsequently found to be in non-compliance, any part of its assigned amount that has been transferred to other Parties under the provisions of Article 17 after the point in time at which the question was raised shall be invalidated and cannot be used for the purpose of meeting commitments under Article 3, or further traded. Such questions can only be raised in particular circumstances to be defined. **(Germany et al.)**

194. [...][7] **(Germany et al.)**

195. The liability to sustain the emission reductions should rest with the entity or state selling the ERU. The degree of sustainability of the ERU should be reflected in its certification and longevity. **(South Africa)**

196. Switzerland has carefully considered the various options to ensure compliance with trading rules (e.g. seller/buyer/shared liability, compliance reserve) and we have come to the conclusion that the so-called post-verification trading approach is likely the administratively simplest, most predictable/low-risk, lowest cost, most transparent and most environmentally credible approach, since over-selling is essentially impossible and therefore no liability stipulations are required. **(Switzerland)**

197. Under this system, Parties/entities can only trade average annual PAA units available (averaged over the 5 years of the commitment period) in excess of their actual emission inventories for the previous year (under this model, trading could begin only in 2009 or as soon as the inventory for 2008 is available). If this option is selected, only those Parties that have excess annual average PAAs as compared to actual emissions in the previous year can trade and the amount that can be traded is limited to this excess. Certificates for these excess PAA units

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[7] Text will be provided at a later stage.

could be issued annually to each Party by the secretariat, if the Article 8 review process raised no question of implementation related to the quality of the emission inventory of the Party in question. Parties issued PAA unit certificates could choose to retain them for ensuring compliance with their obligations under Article 3, to auction them to legal entities under their jurisdiction (grandfathering should not be permitted, due to the risk of trade distortions) or to sell them to other eligible Parties or legal entities. Under this system, there would be no risk of over-selling and thus no need for complicated liability and non-compliance procedures that represent a high risk to the private sector. **(Switzerland)**

O. Implementation

198. "Transfers and acquisitions' of any emission reduction units or any part of an assigned amount could be effected through bilateral or multilateral arrangements between or among Parties included in Annex B, without creating a new international business transaction system or regime. **(China)**

199. If a question of implementation by a Party included in Annex B of the requirements referred to in these principles, modalities, rules and guidelines is identified in accordance with the relevant provisions of Article 8, transfers and acquisitions of parts of assigned amount may continue to be made after the question has been identified provided that such parts of assigned amount may not be used by a Party to meet its commitments under Article 3 until any issue of compliance has been resolved in favour of the Party in question. **(Germany et al.)**

200. Transfers and acquisitions of part of an assigned amount between Parties may take place through an exchange. This exchange shall also be open to legal entities. **(Germany et al.)**

201. Any Party wishing to transfer or acquire any part of an assigned amount must publish the amount to be transferred prior to the transfer. **(Germany et al.)**

202. The secretariat shall make information on the Parties that are eligible to participate in international trade publicly available. Each Party shall maintain a record of names and contact details of authorized legal entities within its jurisdiction that it authorizes to trade, and such information shall be made available both to the secretariat and to the public. **(Germany et al.)**

203. [...][8] **(Germany et al.)**

P. Supplementarity

204. AOSIS believes that the use of mechanisms by any Annex I Party has to be supplemental to its domestic action. Quantitative and qualitative rules and guidelines on supplementarity may be developed in the context of the elaboration of the Kyoto Protocol Articles 2 and 3.2. These binding commitments on policies and measures and on demonstrable progress would be

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[8] Text will be provided at a later stage.

seriously undermined if Annex I Parties were allowed to fulfil their obligations under Article 3 of the Kyoto Protocol primarily through extraterritorial means. **(AOSIS)**

205. Rules on supplementarity should be developed in the context of these Articles and subject to the Protocol's reporting, in-depth review and non-compliance procedures, which should be empowered to suspend the right of a Party to access mechanisms in circumstances where it has failed to demonstrate that its domestic efforts form the primary means of achieving its quantified emissions reduction limitation commitments. **(AOSIS)**

206. AOSIS is concerned, however, that an overdependence of certain Annex I Parties on the use of the Protocol mechanisms to achieve their commitments may undermine their ability to fulfil commitments domestically, to demonstrate supplementarity, and to undertake more ambitious commitments in the next round of negotiations. **(AOSIS)**

207. With regard to the principle of supplementarity, AOSIS believes that the legal and political character of any RIEO seeking special treatment under the Protocol must be assessed separately, particularly with regard to the division of climate relevant competencies between the central authority and its member states. **(AOSIS)**

208. AOSIS strongly supports the concept of supplementarity and welcomes any proposals as to how it might be determined on either a quantitative or qualitative basis. **(AOSIS)**

209. The "emissions trading" (ET) under Article 17 of the Kyoto Protocol is a very limited kind of "trading". As clearly provided for in Article 17 of the Kyoto Protocol, "Any such trading shall be supplemental to domestic actions for the purpose of meeting quantified emission reduction commitments" under Article 3 of the Kyoto Protocol. The purpose of the "emissions trading" under Article 17 is to assist Parties included in Annex B in fulfilling their commitments under Article 3, as a supplementary means. **(China)**

210. This means that the nature, purposes and scope of the ET under Article 17 are essentially no other than being supplemental to domestic actions **for** meeting Annex B Parties' quantified limitation and reduction commitments under Article 3 of the KP - not for international speculation, etc. **(China)**

211. On this principle, the Kyoto Protocol has clear provisions relating to the 3 mechanisms. Specifically, regarding ET, Article 17 stipulates: "Any such trading shall be supplemental to domestic actions for the purpose of meeting quantified emission limitation and reduction commitments" under Article 3 of the KP. Therefore, concrete ceiling for the total amount of overseas offsetting acquired from the 3 mechanisms of the Kyoto Protocol should be defined quantitatively and qualitatively. (See: **Elements** No. 9 under Article 12, No. 19 under General, No. 6 under Article 6, and No. **8** under Article 17 - as listed in the **"Work Programme"**, annexed to COP decision 7/CP.4. (Doc. FCCC/CP/1998/16Add.1). **(China)**

212. [...][9] **(Germany et al.)**

213. At no time should Annex I Parties be allowed to fulfill their obligations to Kyoto Protocol only by using facilities provided in other countries. The use of flexibility mechanisms by Annex I Parties has been supplemental to domestic ones. **(Mauritius)**

214. The use of mechanisms through the countries listed in Annex B shall be supplemental to their domestic action. **(Sierra Leone)**

215. The mechanisms should be supplemental to domestic action, however the extent of this supplementarity is dependent on the conditions attached to the mechanisms. If developing countries are able to bank credits and activities for long-term application, the mechanisms can be used to a major extent. Failing this, the major benefits go to developed countries and the use of mechanisms should be constrained. The question of the extent to which Article 3 commitments should be achieved through domestic action should be considered on a flexible basis so that achievement of the commitment makes the most efficient use of all available mechanisms of which domestic action is one. The question of equity will need to be discussed here as well. Consideration does however need to be given to the introduction of flexibility in the allocations to different mechanisms, especially as a function of time and as changing technologies, development rates and cost structures present new opportunities. As such some means of revising these allocations needs to be established. This can only be achieved if the value of the credits are comparable. In the case of the CDM the fact that the mechanism should provide for a percentage for adaptation should be built into the value so that the value of these credits is not inferior to those from the other two mechanisms. **(South Africa)**

216. Application of any quantification of "supplemental to domestic actions" to each individual State within a regional economic integration organization. Apply as per Annex B. **(South Africa)**

217. Lack of authority to elaborate "supplemental to domestic actions"; inadvisability of doing so. It is desirable to include domestic action to avoid exploitation of short term opportunities – especially in economies in transition, in exchange for long-term high costs. As such, the mechanisms should be supplemental to domestic action. However, the extent of this supplementarity is dependent on the conditions attached to the mechanisms. If developing countries are able to bank credits and activities for long-term application, the mechanisms can be used to a major extent. Failing this, the major benefits go to developed countries and the use of mechanisms should be constrained. **(South Africa)**

218. Uganda is a least developed country and among the most vulnerable countries to adverse effects of climate change. It therefore strongly believes that reduction of greenhouse gases under the Convention and the Protocol must be primarily done within Annex I Party territories. In this regard offshore activities leading to reductions or avoidance of GHGs must be supplemental. Level of domestic reduction and offshore reductions or avoidance must be quantified. Also due

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[9] Text will be provided at a later stage.

attention must be paid to the quality of credits resulting from offshore reduction, avoidance or sequestration. Discussions of the quantification should proceed in parallel with the discussions on design of the flexible mechanisms. Uganda is looking forward to discussions of these principles. **(Uganda)**

Q. Issues related to compliance

219. Rules on supplementarity should be developed in the context of these Articles and subject to the Protocol's reporting, in-depth review and non-compliance procedures, which should be empowered to suspend the right of a Party to access mechanisms in circumstances where it has failed to demonstrate that its domestic efforts form the primary means of achieving its quantified emissions reduction limitation commitments. **(AOSIS)**

220. AOSIS wishes to express strong support for the establishment, under Article 18 of the Kyoto Protocol, of 'appropriate and effective procedures and mechanisms to determine and to address cases of non-compliance with the provisions of this Protocol, including through the development of an indicative list of consequences, taking into account the cause, type, degree and frequency of non-compliance.' Included among these consequences must be the authority to suspend the ability of any non-complying Party to benefit from participation in the Protocol's mechanisms. **(AOSIS)**

221. AOSIS believes the mechanisms can play a central role in promoting compliance by offering cost-effective means of emissions reductions, by encouraging the transfer of financial resources and technology, and engaging the private sector and developing countries in the business of reducing greenhouse gas emissions. **(AOSIS)**

222. Conditioning the access of Parties to the benefits of participating in the mechanisms on their demonstrating compliance with Protocol obligations will also provide powerful incentive. **(AOSIS)**

223. Linking participation in the emissions trading regime with compliance with Articles 5 and 7 would have the ancillary benefit of promoting compliance with key obligations under the Protocol. It is through these articles that Parties will demonstrate compliance with their quantified emission limitation and reduction commitments. Assessing compliance with such commitments indeed depends upon proper implementation of these articles. **(Australia et al.)**

224. It is assumed that there would be a short period after the end of a commitment period during which Parties would have the opportunity to cure any overage, e.g., through acquiring units of assigned amount. One issue is whether, after that short period, a Party whose emissions exceeded its assigned amount for the previous commitment period should retain its eligibility to participate in emissions trading under Article 17 in the subsequent commitment period. **(Australia et al.)**

225. These end-of-commitment-period issues merit further consideration, taking into account discussions on the overall non-compliance regime. **(Australia et al.)**

226. At the end of each commitment period, there shall be a [short time period] during which Parties have the opportunity to cure any emissions overage, e.g., through acquiring units of assigned amount. [Need to address issue of whether a Party whose emissions (after the short period) exceeded its assigned amount for the previous commitment period should retain its eligibility to participate in emissions trading under Article 17 in the subsequent commitment period.] **(Australia et al.)**

227. Compliance. Use standard systems to measure compliance – with clearly defined interpretation of the targets set – indicating tons to be met over the Kyoto Protocol compliance period. The measure of compliance is then emissions over this period minus the total of credits held by that Party. It is therefore clear that any Party with targets needs to put a system in place to track credits held in its territory, some form of central bank which tracks transactions in both CERs and ERUs. Penalties for non-compliance should be negotiated under Articles 12 and 17 rather than Article 18. **(South Africa)**

228. Compliance-related issues. These are the same for all mechanisms and include: Emission reduction quantification; Life times of credits; Ownership, trading, banking; Application of credits against targets. **(South Africa)**

229. Switzerland believes that – for each of the three Kyoto Mechanisms – there is a need for independent validation/certification. Under Article 6, each project must be validated to ensure that it meets the project eligibility criteria and has a baseline that meets agreed standards, and the resulting emission reductions must be certified after they have occurred. The same basic validation/certification requirements generally hold true for Article 12, as well. Under Article 17, the national systems for the preparation of emission inventories must be validated[10] to conform with the guidelines to be decided upon by the COP/MOP and, in the case that legal entities are authorized to participate in emissions trading, national systems for accurate tracking and accountability of trading activity by legal entities must also be validated to ensure that they meet the requirements to be specified under the rules for Article17. Furthermore the amount of excess PAA units available to a Party must be certified – and certificates issued – annually (assuming a post-verification trading system). **(Switzerland)**

230. Building on existing know-how and institutions, the generally local independent "operational entities" (borrowing the terminology from the Kyoto Protocol for the CDM) could be accredited to perform the necessary validations/certifications by existing national or regional accreditation authorities designated by the COP/MOP. In the case of the CDM, Article 12.5 states that the operational entities are to be designated by the COP/ MOP, but this "designation" could occur via national/regional accreditation authorities to avoid an administrative bottleneck. We would welcome discussion of this and other possible approaches at the upcoming sessions of SBSTA/SBI. For the other Mechanisms, operational entities are not explicitly mentioned, but will be needed if validation / certification is required, as we propose above. **(Switzerland)**

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[10] It is essential for the credibility of the emissions trading system that national emission inventory systems/data be validated by an accredited independent instance. Otherwise there is huge room for falsification of inventory data, since uncertainties of 50-100 per cent or more are not uncommon.

231. Operational entities must be accredited by designated national/regional authorities to perform validation/certification on the basis of a set of protocols (or standards) for validation or certification. These validation and certification protocols must by adopted by the COP/MOP. In the case of emission trading and joint implementation, the Secretariat might be tasked with actually issuing certificates based on the certification report by the operating entity, whereas this task might be performed under the CDM by the executive board. **(Switzerland)**

232. If such a system is established, it would only apply to those Parties that choose to engage in the Kyoto Mechanisms, and would have to be linked to the entire system for measurement, reporting, review and compliance under the Protocol (including the expert review process under Article 8, which applies only to Annex I countries). The review process in Article 8.1 and the expert reviews under Article 8.2 might be used to spot check the performance of the operational entities acting in those Annex I Parties engaging in JI, CDM or emissions trading. The Article 8 reviews, however, could not replace the verification/certification process for the Kyoto Mechanisms. **(Switzerland)**

233. Switzerland has carefully considered the various options to ensure compliance with trading rules (e.g., seller/buyer/shared liability, compliance reserve) and we have come to the conclusion that the so-called post-verification trading approach is likely the administratively simplest, most predictable/low-risk, lowest cost, most transparent and most environmentally credible approach, since over-selling is essentially impossible and therefore no liability stipulations are required. **(Switzerland)**

234. Under this system, Parties/entities can only trade average annual PAA units available (averaged over the 5 years of the commitment period) in excess of their actual emission inventories for the previous year (under this model, trading could begin only in 2009 or as soon as the inventory for 2008 is available). If this option is selected, only those Parties that have excess annual average PAAs as compared to actual emissions in the previous year can trade and the amount that can be traded is limited to this excess. Certificates for these excess PAA units could be issued annually to each Party by the Secretariat, if the article 8 review process raised no question of implementation related to the quality of the emission inventory of the Party in question. Parties issued PAA unit certificates could choose to retain them for ensuring compliance with their obligations under Article 3, to auction them to legal entities under their jurisdiction (grandfathering should not be permitted, due to the risk of trade distortions) or to sell them to other eligible Parties or legal entities. Under this system, there would be no risk of over-selling and thus no need for complicated liability and non-compliance procedures that represent a high risk to the private sector. **(Switzerland)**

R. Periodic Review

235. The COP shall review the principles, modalities, rules and guidelines governing the operation of the emissions trading system, as set out in paragraphs 1-11 of the submission (see document FCCC/SB/1999/MISC.3). The first review shall be carried out no later than the year 2012. Further reviews shall be carried out periodically thereafter. **(Germany et al.)**

236. Changes in principles, modalities, rules and guidelines shall take effect in commitment periods subsequent to that of their adoption. Changes in Parties' eligibility to trade or changes pertaining to new entrants that meet the eligibility criteria may occur during the current commitment period. **(Germany et al.)**

S. Further work

237. The proposal by the European Community and its member States, and Bulgaria, Croatia, the Czech Republic, Hungary, Latvia, Poland and Slovenia does not cover all of the issues that need to be addressed. We are looking forward to a fruitful discussion also on the following questions:

(a) How can environmental effectiveness be ensured?

(b) How can transparency, accessibility and verifiability be ensured?

(c) Should parts of the assigned amount units be retired annually?

(d) How can emissions trading serve as an incentive for compliance ?
(Germany et al.)

T. Capacity-building

238. Participation in any of the mechanisms under the Kyoto Protocol will require substantial capacity in both the 'transferring' and the 'acquiring' countries, particularly in developing and least developed countries. Experience from the AIJ pilot phase, and from the domestic use of similar 'mechanisms', demonstrates that sophisticated means of monitoring, reporting and verifying emissions will be required of any country wishing to host or transfer emissions reductions. **(AOSIS)**

239. AOSIS believes that the existence of this capacity must be demonstrated as a prerequisite for participating in the mechanisms, and that resources should be made available to eligible Parties to meet the costs of building such capacity. **(AOSIS)**

240. AOSIS further considers it to be necessary to establish a specific mechanisms to assist developing countries with the capacity-building required for these countries to be able to participate in the CDM. Such a mechanism should be established well in advance of the implementation of the Kyoto Protocol mechanisms. **(AOSIS)**

241. Capacity-building. This should be an integral component of the application of the mechanisms and should include equitable capacity-building in all developing countries.
(South Africa)

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